

DEPARTMENT OF STATE REVENUE
LETTER OF FINDINGS: 03-0309
Indiana Gross Retail Tax
For the Years 1999 and 2000

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of the document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUES

I. Use Tax Exemption – Shipping Blocks.

Authority: IC 6-2.5-5-9(d); 45 IAC 2.2-5-16; 45 IAC 2.2-5-16(a); 45 IAC 2.2-5-16(c)(1); 45 IAC 2.2-5-16(d)(1).

Taxpayer argues that it was not required to pay sales tax when it purchased shipping blocks ("chocks") on the ground that the chocks are "wrapping materials" exempt from taxation.

II. Abatement of the Ten-Percent Negligence Penalty.

Authority: IC 6-8.1-10-2.1; IC 6-8.1-10-2.1(d); 45 IAC 15-11-2(b); 45 IAC 15-11-2(c)(1);

Taxpayer asks that the Department of Revenue (Department) exercise its discretion to abate the ten-percent negligence penalty assessed following completion of the original audit review.

STATEMENT OF FACTS

Taxpayer is an out-of-state company in the business of developing, manufacturing, marketing, and distributing copper, aluminum, and fiber optic cable. Taxpayer operates out of various locations including locations within Indiana. Taxpayer's products are sold to and used by the communications, energy, industrial, and specialty markets.

The Department conducted an audit review of taxpayer's business and tax records. As a result of that audit, the Department determined that taxpayer owed additional gross retail (use) taxes. Accordingly, the Department sent taxpayer notices of "proposed assessment" which included the additional amount of tax and imposition of the ten-percent negligence penalty. Taxpayer disagreed with the audit results and submitted a protest to that effect. An administrative hearing was conducted during which taxpayer's representative further explained the basis for the protest. This Letter of Findings results.

DISCUSSION

I. Use Tax Exemption – Shipping Blocks.

Taxpayer bought wooden blocks without paying sales tax. When the audit division reviewed taxpayer's records, it decided that taxpayer should have paid sales tax on these purchases. Accordingly, the audit assessed use tax on the purchases on the ground that the purchase of the blocks was not exempt from sales tax.

When taxpayer ships its cable products to customers, the cables are wound on steel or wooden reels. Depending on the nature of the cable, the reels may be wrapped in bubble-wrap or shrink-wrap. When the reels are loaded for transport to the customer, taxpayer fastens these wooden, wedge-shaped blocks to the outer rim of each reel. The wedge-shaped blocks serve to keep the reels from moving during shipment. After the reels are delivered to the customer, the blocks are removed by the customer and discarded; the blocks are not reused, and the blocks are not returned to taxpayer.

Taxpayer argues that these blocks are exempt for sales/use tax pursuant to IC 6-2.5-5-9(d) which states:

Sales of wrapping material and empty containers are exempt from the state gross retail tax if the person acquiring the materials or containers acquires them for use as nonreturnable packages for selling the contents that he adds.

The Department's regulation, 45 IAC 2.2-5-16, interprets the extent of the exemption set out in IC 6-2.5-5-9(d). The regulation states that, "The state gross retail tax shall not apply to sales of nonreturnable wrapping materials and empty containers to be used by the purchaser as enclosures or containers for selling contents to be added, and returnable containers containing contents sold in a sale constituting selling at retail and returnable containers sold empty for refilling." 45 IAC 2.2-5-16(a). Under this regulation, "Nonreturnable containers and wrapping materials [include] steel strap and shipping pallets to be used by the purchaser as enclosures for selling tangible personal property." 45 IAC 2.2-5-16(c)(1). In order to qualify for the exemption as a nonreturnable container or wrapping material, "The purchaser must add contents to the containers purchased; and the purchaser must sell the contents added." 45 IAC 2.2-5-16(d)(1).

It is clear that the wooden blocks are not returned to taxpayer and are, therefore, "nonreturnable." It is also clear that the wooden blocks are associated with sales of taxpayer's cable in transactions which constitute "selling at retail." Based on taxpayer's description, it is clear that the wooden blocks are a necessary – if not essential – aid in shipping the reels of cable. However, the blocks are not exempt from the state's gross retail tax because taxpayer does not "add contents to the containers purchased." IC 6-2.5-5-9(d) permits an exemption for nonreturnable items to which the taxpayer adds "contents." Taxpayer's blocks are used to facilitate the shipping of the reels, but they are not "enclosures or containers" into which taxpayer adds its product.

FINDING

Taxpayer's protest is respectfully denied.

II. Abatement of the Ten-Percent Negligence Penalty.

The audit imposed a ten-percent negligence penalty presumably on the ground that taxpayer failed to pay sales tax on certain taxable transactions and, thereafter, failed to self-assess use tax. Taxpayer argues that the negligence penalty is inappropriate because, although it admittedly failed to self-assess use tax on a number of taxable purchases, given the scope of taxpayer's multi-state business operations, the number of transactions it enters into each year, and the comparatively small number of transactions which the audit found were taxable, it did not act in a negligent manner.

IC 6-8.1-10-2.1 requires that a ten-percent penalty be imposed if the tax deficiency results from the taxpayer's negligence. Departmental regulation 45 IAC 15-11-2(b) defines negligence as "the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer." Negligence is to "be determined on a case-by-case basis according to the facts and circumstances of each taxpayer." Id.

IC 6-8.1-10-2.1(d) allows the Department to waive the penalty upon a showing that the failure to pay the deficiency was based on "reasonable cause and not due to willful neglect." Departmental regulation 45 IAC 15-11-2(c) requires that in order to establish "reasonable cause," the taxpayer must demonstrate that it "exercised ordinary business care and prudence in carrying out or failing to carry out a duty giving rise to the penalty imposed"

Without excusing the taxpayer's initial failure to appropriately self-assess use taxes on all of its 1999 and 2000 transactions, the Department concludes that taxpayer's failure to exercise "ordinary business care" in neglecting to self-assess use tax on a limited number of transactions, does not necessitate imposition of the negligence penalty. The penalty should be abated in its entirety.

FINDING

Taxpayer's protest is sustained.